REALVEST PROPERTIES SDN. BHD.

v.

THE CO-OPERATIVE CENTRAL BANK LIMITED (UNDER RECEIVERSHIP)

FEDERAL COURT, KUALA LUMPUR
DATO' CHONG SIEW FAI CJ (SABAH & SARAWAK)
DATO' PEH SWEE CHIN FCJ
DATO' MOHAMED DZAIDDIN ABDULLAH FCJ
[CIVIL APPEAL NO: 02-207-92]
30 JANUARY 1996

BANKING & FINANCE: *Loan – Interest – Charging of additional interest upon default – Legality – Whether a penalty and therefore irrecoverable – Whether only liquidated damages – Proper test – Co-operative Societies Act 1948 s. 30 – Contracts Act 1950 s. 75.*

CONTRACT: *Loan agreement – Default by borrower – Payment of separate interest by reason of default – Whether contravened s. 75 Contracts Act 1950 – Whether additional interest a penalty – Whether irrecoverable – Whether only liquidated damages – Difference between penalty and liquidated damages – Test.*

CO-OPERATIVE SOCIETIES: *Registered society – Power to give loans to members – Section 30(1)(a) Co-operative Societies Act 1948 – Loan granted to a member to be utilised by a third party – Whether void.*

The respondent is a Co-operative Society established under the Co-operative Societies Act 1948. Upon a security provided by the appellant, the respondent granted a loan to its member by the name of Khalid. The facts however showed that, although Khalid was the borrower, the loan was in fact taken and utilised by Kemajuan Perkasa Sdn. Bhd. of which Khalid was an agent. That apart, it was also common ground that, aside from the the prescribed 14.5% interest rate principally attached to the loan, a clause (clause 3.2) was annexed to the relevant charge instrument stating that upon default, a separate default interest of 20% per annum was chargeable "on the sum in arrears calculated retrospectively from the due date of such default until the date of payment of the amount thereof".

Khalid defaulted in the payment of the loan, and the land was subsequently sold off by public auction, following the issuance of the statutory order for sale. In this appeal, the appellant sought to challenge the legality of the order of sale, arguing in effect (i) that the charge was void as the loan contravened s. 30 Co-operative Societies Act 1948 and (ii) that the additional interest contravened s. 75 of the Contracts Act 1950, and so, was *ultra vires* and irrecoverable. The primary issues that arose were:

(i) whether the charging of additional interest herein amounted to a penalty within the meaning of s. 75 Contracts Act 1950, and so, was irrecoverable.

(ii) whether in any event, and bearing in mind the said s. 75 (ie, illustration (d) thereof), the chargee is entitled to receive a reasonable compensation not exceeding the stipulated penalty.

Held:

Peh Swee Chin FCJ (delivering the judgment of the Court):

[1] There is nothing objectionable to the respondent granting the loan to Khalid who after all is one of its members. Section 30 of the Co-operative Societies Act 1948 does not specify to what purpose such a loan should be utilised, and likewise, there is nothing objectionable to Khalid using the loan granted by the plaintiff for the benefit of Kemajuan Perkasa Sdn. Bhd. As lending money to its member like Khalid must be one of the objects of the respondent, the loan is valid and is enforceable against the appellant, the chargor, who provided the security for the loan.

[2] Given its ordinary and natural meaning, clause 3.2 would mean, *prima facie*, that under it, another separate, distinct or additional amount of interest will be demanded on a sum in arrear (such sum itself comprised principal and capitalised interest), in addition to an anterior and earlier amount of interest provided in clause 3.1. That this is so in reality is however confirmed from the evidence as well as from the submission of learned Counsel for the chargee.

[3] The essence of a penalty is a stipulated payment *in terrorem* of the party breaching whereas in liquidated damages, it is a genuine pre-estimate by both parties of the damages for such breach of contract.

[4] Bearing in mind s. 75 of the Contracts Act, a stipulation for default interest may or may not be a penalty depending on circumstances. Illustration (d) to the section however gives rise to a clear implication that default interest rate, in order to be caught by s. 75, must be exorbitant.

[5] The above notwithstanding, having regard to the *ratio* of the Privy Council decision in *Sundar Koer v. Sham Kishen*, a default or additional interest, even if not exorbitant, would still amount to a penalty, and therefore void, if the interest were calculated from the date of the charge and not from the date of default, and if the additional money payment became immediately payable by the chargor. As it is, such default interest is harsh and unconscionable.

[6] The provisions of written law in s. 75 of the Contracts Act 1950 are not capable of supplanting *in toto* the common law on the question of penalty and liquidated damages. This being the case, in construing the effect of the provision of default interest in a contract, specific provision such as the "Explanation" in s. 75 would have to be interpreted according to common law, as to whether it is liquidated damages or a penalty (though subject to the provisions of the said s. 75).

[7] In the present case, the element of "additional money payment" was involved, in that, on default, a default interest of 20% per annum, chargeable separately and additionally on arrears comprising principal and interest, became payable. It was also clear that this default interest was paid side by side with the interest calculated by prescribed rate of 14.5% on the same money lent or owed for the same span of time. In the circumstances, clause 3.2 of the annexure to the charge in question is void and unenforceable by virtue of s. 75 of the Contracts Act 1950 and the interest calculated by virtue of the said clause 3.2 is irrecoverable.

[8] In a default such as happened here, there is an established measure of damages payable by a borrower which is damages for loss of use of fund or money. This was due to the fact that the sum in arrear, if it had not been in arrear and had been paid back punctually to the chargee, could have been lent to some other person by the chargee at certain interest for the period while it was in arrear. However, in this case, damages for the loss of use of such money has not been proved, so that the Court cannot make any award in regard to it.

[9] In view of the Court finding clause 3.2 void and the said failure to prove damages for loss of use of the money in question, the default interest charged by virtue of the said clause 3.2 would have to be deducted from the amount of repayment to the chargee by the chargor.

[Appeal dismissed upon certain terms and conditions]

***[Bahasa Malaysia** Translation of Headnotes]*

***PERBANKAN & KEWANGAN:** Pinjaman – Faedah – Pengenaan faedah tambahan setelah mungkir – Keesahan – Samada merupakan satu penalti dan dengan itu tidak dapat diperolehi – Samada hanya gantirugi jumlah tertentu – Ujian wajar – Akta Koperasi 1948 s. 30 – Akta Kontrak 1950 s. 75.*

***KONTRAK:** Perjanjian pinjaman – Kemungkiran oleh peminjam – Pembayaran faedah berasingan disebabkan oleh kemungkiran – Samada melanggari s. 75 Akta Kontrak 1950 – Samada faedah tambahan merupakan satu penalti – Samada boleh diperolehi – Samada hanya gantirugi jumlah tertentu – Perbezaan antara penalti dan liquidated damages – Ujian.*

KOPERASI: *Pertubuhan berdaftar – Kuasa untuk memberikan pinjaman kepada ahli – Seksyen 30(l)(a) Akta Koperasi 1948 – Pinjaman diberikan kepada ahli hendaklah digunakan oleh pihak ketiga – Samada tak sah.*

Responden adalah sebuah Pertubuhan Koperasi yang ditubuhkan di bawah Akta Koperasi 1948. Di atas satu jaminan yang diberikan oleh perayu, responden telah memberikan pinjaman kepada ahlinya bernama Khalid. Fakta-fakta namun begitu menunjukkan bahawa, walaupun Khalid merupakan peminjam, pinjaman tersebut pada hakikatnya telah diambil dan digunakan oleh Kemajuan Perkasa Sdn. Bhd. bagi yang mana Khalid adalah seorang ejen. Selain itu, ianya tidak disangkal bahawa, selain daripada kadar faedah yang ditentukan sebanyak 14.5% yang secara utamanya dikenakan pada pinjaman tersebut, satu fasal (fasal 3.2) telah dilampirkan kepada suratcara gadaian yang relevan yang menyatakan bahawa bila berlaku kemungkiran, faedah kemungkiran yang berasingan sebanyak 20% setahun boleh dikenakan "on the sum in arrears calculated retrospectively from the due date of such default until the date of payment of the amount thereof."

Khalid telah memungkiri pembayaran pinjaman tersebut, dan tanah itu telah kemudiannya dijual melalui perlelongan awam, berikutan dengan perintah berkanun yang dikeluarkan bagi penjualan tersebut. Dalam rayuan ini, perayu mencabar keesahan perintah jualan tersebut, berhujah secara berkesannya (i) bahawa gadaian tersebut tak sah kerana pinjaman tersebut telah melanggari s. 30 Akta Koperasi 1948 dan (ii) bahawa faedah tambahan melanggari s. 75 Akta Contract 1950, dan dengan itu, adalah *ultra vires* dan tidak dapat diperolehi. Isu-isu utama yang berbangkit adalah:

(i) samada pengenaan faedah tambahan di sini membawa kepada satu penalti dalam maksud s. 75 Akta Kontrak 1950, dan dengan itu, adalah tidak dapat diperolehi.

(ii) samada dalam apa keadaanpun, dan mengambil perhatian akan s. 75 (iaitu ilustrasi (d) di situ), pemegang gadaian adalah berhak untuk menerima pampasan yang wajar tidak melebihi penalti yang ditetapkan.

Diputuskan:

Oleh Peh Swee Chin HMP (menyampaikan penghakiman Mahkamah):

[1] Tidak terdapat apa-apa yang boleh dibantah mengenai pemberian pinjaman oleh responden kepada Khalid yang merupakan seorang ahlinya. Seksyen 30 Akta Koperasi 1948, tidak menentukan bagi tujuan apa pinjaman sedemikian seharusnya digunakan, dan begitu juga, tidak terdapat apa-apa yang menghalang Khalid menggunakan pinjaman yang telah diberikan oleh plaintif demi kebaikan Kemajuan Perkasa Sdn. Bhd. Oleh kerana meminjam wang kepada ahli-ahlinya seperti Khalid adalah merupakan salah satu tujuan responden, maka pinjaman tersebut adalah sah dan berkuatkuasa

terhadap perayu, iaitu penggadai, yang telah memberikan jaminan bagi pinjaman tersebut.

[2] Menurut maksud asal dan biasa, fasal 3.2 akan bermaksud, *prima facie*, bahawa di bawahnya, satu lagi faedah yang berasingan, berbeza atau tambahan akan dituntut ke atas jumlah tertunggak (jumlah yang sedemikian adalah terdiri daripada jumlah pokok serta faedah yang menjadi terakru), sebagai tambahan jumlah faedah yang sebelumnya dan yang terdahulu yang diberikan dalam fasal 3.1. Bahawa perkara ini adalah sedemikian rupa disahkan daripada keterangan dan juga dari penghujahan Peguam yang bijaksana bagi pihak pemegang gadaian.

[3] Intipati sesuatu penalti adalah pembayaran yang ditentukan *in terrorem* oleh pihak yang melakukan kemungkiran sedangkan dalam gantirugi jumlah tertentu, ianya adalah anggaran terdahulu oleh kedua-dua pihak akan gantirugi bagi kemungkiran kontrak yang sedemikian.

[4] Mengambil perhatian akan s. 75 Akta Kontrak, satu penetapan bagi kemungkiran faedah boleh atau mungkin tidak merupakan satu penalti bergantung kepada keadaannya. Ilustrasi (d) kepada seksyen itu namun begitu membangkitkan petanda yang jelas bahawa kadar faedah kemungkiran, agar ianya termasuk dalam s. 75, mestilah keterlaluan.

[5] Tanpa menghiraukan perkara yang tersebut di atas, dalam menimbang *ratio* keputusan Majlis Privi dalam *Sundar Koer v. Sham Kishen*, sesuatu kemungkiran faedah tambahan, walaupun tidak keterlaluan, akan merupakan satu penalti, dan dengan itu adalah tak sah, jika faedah tersebut dikira daripada tarikh gadaian dan bukannya daripada tarikh kemungkiran, dan jika pembayaran wang tambahan menjadi kena dibayar dengan serta merta oleh penggadai. Sepertimana keadaannya, faedah kemungkiran yang sedemikian adalah keterlaluan dan tidak berpatutan.

[6] Peruntukan undang-undang bertulis dalam s.75 Akta Kontrak 1950 tidak berkeupayaan mengambil tempat *in toto* common law berhubung dengan persoalan penalti dan gantirugi jumlah tertentu. Oleh yang demikian, dalam mentafsirkan kesan peruntukan kemungkiran faedah dalam sesuatu kontrak, peruntukan yang tertentu seperti "Expnanation" dalam s. 75 hendaklah ditafsirkan menurut common law, iaitu samada ianya adalah gantirugi jumlah tertentu atau satu penalti (walaupun tertakluk kepada peruntukan tersebut s. 75 tersebut).

[7] Dalam kes semasa ini, unsur "additional money payment" terlibat, iaitu, ketika mungkir, satu faedah kemungkiran sebanyak 20% setahun, yang dikenakan berasingan dan secara tambahan ke atas tunggakan yang terdiri daripada jumlah pokok dan faedah, menjadi kena dibayar. lanya adalah juga jelas bahawa faedah kemungkiran ini dibayar berserta dengan faedah yang dihitung pada kadar yang ditentukan sebanyak 14.5% ke atas wang yang

sama yang telah dipinjamkan atau terhutang bagi tempoh masa yang sama. Dalam keadaan yang sedemikian, fasal 3.2 lampiran kepada gadaian yang menjadi persoalan adalah tak sah dan tidak boleh dikuatkuasakan menurut s. 75 Akta Kontrak 1950 dan faedah yang dihitung menurut fasal 3.2 tersebut tidak dapat diperolehi.

[8] Dalam sesuatu kemungkiran sepertimana yang berlaku di sini, terdapat pengiraan tetap bagi gantirugi yang kena dibayar oleh sipeminjam yang mana adalah gantirugi bagi kehilangan hak penggunan dana atau wang. Ini adalah disebabkan hakikat bahawa wang yang tertunggak, jika ianya tidak tertunggak, dan telah dibayar balik dengan tepatnya kepada pemegang gadaian, boleh dipinjamkan kepada seorang yang lain oleh pemegang gadaian pada kadar faedah yang tertentu bagi tempoh ketika ianya berada dalam tunggakan. Walaubagaimanapun, dalam kes ini, gantirugi bagi kehilangan hak menggunakan wang yang sedemikian telah tidak dibuktikan, dan Mahkamah tidak boleh membuat apa-apa award berhubung dengannya.

[9] Memandangkan bahawa Mahkamah telah memutuskan fasal 3.2 tak sah dan kegagalan untuk membuktikan kehilangan hak kegunaan wang yang dipersoalkan itu, faedah kemungkiran yang dikenakan menurut fasal 3.2 haruslah ditolak daripada jumlah pembayaran balik kepada pemegang gadaian oleh penggadai.

[Rayuan ditolak atas terma-terma dan syarat-syarat tertentu]

Cases referred to:
The Co-operative Central Bank v. Gayabaru Construction ***(refd)***
Dunlop Pneumatic Tyre Co v. New Garage & Motor Co [1915] AC 79 ***(refd)***
Phonographic Equipment v. Muslu [1961] 1 WLR 1379 ***(refd)***
Sundar Koer v. Sham Kishen [1906] 34 1 A 917 ***(refd)***

Legislation referred to:
Contracts Act 1950, s. 75
Co-operative Societies Act 1948, s. 30

For the appellant - Renu Zechariah; M/s. Anad & Assoc.
For the respondent - S Gunavathi; M/s. Nazri Aziz & Wong

JUDGMENT

Peh Swee Chin FCJ:

This appeal brings into focus some problems, *inter alia*, as to whether the charging of additional interest by a bank for default by a borrower is caught by s. 75 of the Contracts Act, 1950. First, a brief summary of facts and events leading to this appeal will have to be set out. The bank, (the respondent/plaintiff) in this instant case is not an ordinary commercial bank but a co-operative society registered under the Co-Operative Societies Act, 1948.

The appellant/defendant was the chargor and the respondent/plaintiff the chargee (hereinafter "the chargor" and "the chargee" respectively) as the case may be). The chargee applied for an order of the sale of land charged to secure money lent to one Khalid bin Ramlee by the chargee. A statutory order of sale was made on 10 April 1992; the charged land was duly sold by public auction and the proceeds of sale had been paid to the chargee pending an appeal against the said order of sale dated 10 April 1992 on several grounds.

First, it was submitted that the charge was void on the ground that though the loan of RM3 million in question was made to one Khalid bin Ramlee, a member of the co-operative society, which was the chargee in this case, it was in fact a loan taken and utilized by a company called Kemajuan Perkasa Sdn. Bhd. of which the said Khalid bin Ramlee was an agent, a fact known to the chargee at all material times, (the company is hereinafter referred to as "the said company"). The said company was the actual borrower, the said Khalid bin Ramlee, a nominal one, who became a member of the chargee (ie, the Co-operative Bank) for the purpose of obtaining the loan, thereby rendering the loan void for being *ultra vires* by contravening s. 30 of the Co-operative Societies Act, 1948.

Very briefly, the chargee relied on a passage which was accepted by the Court below from an unreported judgment of Siti Norma Yaacob J under the name of *The Co-operative Central Bank v. Gayabaru Construction*, at p. 2, in Kuala Lumpur High Court Originating Summons No. 1085/1985, on similar facts and the passage says:

> Since s. 30(1)(a) of the Act empowers a registered society to make loans to its members, I do not see anything objectionable to the plaintiff granting the loan to Seah who afterall is one of its members. As the section does not specify to what purpose such a loan should be utilised, I also do not see anything objectionable to Seah using the loan granted by the plaintiff for the benefit of the defendant of which he is its managing director. As lending money to Seah must be one of the objects of the plaintiff to which s. 4 of the Act applies, I hold that the loan is valid and is enforceable against the defendant, the chargor, who provided the security for the loan.

We approve the *dictum* as stating the correct legal position on facts there similar to those as found in the present appeal. This thus disposes of the first point.

The further submission for the chargor was to the effect that as Khalid bin Ramlee was an agent of the said company to the full knowledge of the chargee, the party liable to the chargee should have been the said company. The chargor, not being the said company, was not liable. Here, the chargor had expressly and in writing charged the land in question to the chargee in consideration of money lent to the said Khalid bin Ramlee, this argument or evidence of knowledge of agency, described above, tending to contradict or

vary the charge instrument is inadmissible and is without avail to the chargor, which had executed what is commonly known as a "third party".

The 3rd point raised is of considerable importance. It is about additional interest charged by the chargee, or for that matter by any financial institution, for default of a borrower in the payment of any instalment of money lent further and in addition to the interest chargeable already with the stipulated rate prior to such default and continuing to be chargeable normally on such money lent.

The provision for default interest in this case is unusual. First, the relevant clauses as annexed to the instrument of charge (Form 16B), by means of an annexure are as follows:

3.1 **Interest**

> The chargor shall pay to the Bank interest on the loan at the rate of Fourteen Point Five Per Centum (14.5%) per annum on monthly rests (hereinafter referred to as "the Prescribed Rate" which expression shall include such other rate or rates which the Bank may at any time and from time to time stipulate). All interest due to the Bank in respect of the loan shall be kept current.

3.2 **Additional Interest**

> In the event that any amount due under this agreement (whether of principal or interest due under this Article) is not received by the Bank on the due date, the chargor shall pay to the Bank interest at the rate of One and One Third (1-1/3) times the normal ruling rate of interest on the sum in arrears, calculated retrospectively from the due date at such default until the date of the payment of the amount thereof.

3.3. **Variation of Interest Rate**

> Notwithstanding the provisions relating to the rate of interest as hereinbefore provided the Bank shall be entitled at any time and from time to time to vary at its discretion such rate of interest by serving a notice in writing on the borrower and chargor of its intention and such amended rate of interest shall be payable as from the date specified in the said notice. Service of such notice shall be effected in the same manner as a notice demanding payment of the balance due as herein provided.

Looking at clause 3.1, it provides for the 'starting rate' of interest at 14.5% p.a. and also on 'monthly rests'. There is nothing unusual or anything objectionable in this provision, and the same can be said with regard to clause 3.3 a common clause, which provides for right of the bank to vary the rate of interest as stipulated from time to time.

However, one cannot say the same about clause 3.2. Given the ordinary and natural meaning, one has feared that clause 3.2 would mean *prima facie*, that under it, another separate, distinct or additional amount of interest will be

demanded on a sum in arrear, (such sum itself comprises principal and capitalised interest), in addition to an anterior and earlier amount of interest calculated by means of the stipulated normal rate of interest already provided such default normally in the usual course of things.

Such fear was confirmed from the evidence and submission of learned Counsel, that another separate and distinct amount of interest was indeed charged and made payable in addition to the earlier and separate amount of stipulated interest charged and made payable too. We ascertained this fact, twice, if not thrice from learned Counsel for the chargee and in fact our attention was drawn by her to p. 153 of the appeal record (bahagian A, B & C), where for example, in pursuance of the said clause 3.2, such default interest of 20% p.a. charged additionally and separately (ie at 1-1/3% times the normal prescribed rate), was set out therein together with another amount of interest calculated by means of the stipulated rate of interest of 14.5% p.a. seen side by side, both amounts of interest covering the same period of 1 January 1984 to 31 December 1984 and on the same sum in arrear.

It was submitted both in the Court below and before us that such default interest so calculated in pursuance of the said clause 3.2 and as shown in the manner aforesaid was caught by s. 75 of the Contracts Act, 1950 (hereinafter the said s. 75) and was a penalty and therefore irrecoverable.

The relevant part of the said s. 75, thus raised, has to be set out as follows:

> When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for.
>
> Explanation - A stipulation for increased interest from the date of default may be a stipulation by way of penalty.
>
> **Illustrations**
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> (a) ...
>
> (b) ...
>
> (c) ...
>
> (d) A gives B a bond for the repayment of RM1,000 with interest at 12 per cent at the end of six months, with a stipulation that, in case of default, interest shall be payable at the rate of 75 per cent from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the Court considers reasonable.

The said s. 75 has been explained generally by this Court in *Selva Kumar a/l Murugiah v. Thiagarajah a/l Retnasamy* [1995] 3 MLJ 817, for its legal effect and meaning, but the question of increased interest included in the said s. 75 itself was not dealt with as it was not in issue there but the question has to be dealt with now.

There has been a great deal of litigation in India over this section in connection with increased interest for default and to such cases there, we are naturally inclined.

Looking at the section, any increased interest for default may very well be "a sum named in the contract as the amount to be paid in case of such breach ...". However, the *proviso* there, to quote: "Explanation – A stipulation for increased interest from the date of default **may** be a stipulation by way of penalty", was enacted by way of amendment in India, to provide a modification to such a probable interpretation. We of course imported the said s. 75 complete with such amendment in 1950. The meaning is clear, that such a stipulation for default interest, may or may not be a penalty, depending on circumstances. One may ask, 'what circumstances?'. The answer is apparently found, partially at least in illustration (d) as set out above. Such modification, instead of making such default interest through and through a penalty, must have been intended to protect commercial banks which have always been in the habit and business of charging default interest. Commercial banks have to be protected as they are vital to any orderly national commerce, *inter alia.*

We now look at the illustration (d) which refers to default interest being increased from 12% to 75% from date of default. The illustration gives rise to a clear implication that default interest rate must be exorbitant in order that it be caught by the said s. 75.

The reluctance of a large number of Indian Courts to recognize such default interest as anything having the characteristic of "the sum named in the contract as the amount to be paid" on breach and the subsequent amendment by way of such modification mentioned above has this curious result. While the object of enacting the said s. 75 was to abolish the difference between penalty and liquidated damages so that every sum named in the contract to be paid on breach would be treated as unenforceable on the basis of such sum being a penalty in every case, the amendment by way of the said modification brought back such distinction only in the case of interest or default interest, ie increased interest payable on default. This is evident from the wording of the "Explanation" set out above, notably the word "may" and "penalty" therein. The use of the word "penalty" therein must have been deliberate. Thus in construing the effect of the provision of default interest in a contract, such specific provision would still be interpreted according to common law, as to whether it is liquidated damages or a penalty, subject to and qualified by provisions of written law in the said s. 75 ie the "Explanation" and "the

illustration (d)" therein which are, by no means, from their nature, capable of supplanting *in toto* the common law on the questions of penalty and liquidated damages.

It is not proposed to write in detail the difference between liquidated damages and a penalty in a contract but only to skim over it sufficiently for the purpose of this appeal.

The essence of a penalty is a stipulated payment *in terrorem* of the party breaching the contract whereas in liquidated damages, it is a genuine pre-estimate by both parties of the damages for such breach of contract, see eg, *Dunlop Pneumatic Tyre Co. v. New Garage & Motor Co.* [1915] AC 79, 87. In *Phonographic Equipment v. Muslu* [1961] 1 WLR 1379 & 1387, a contention was raised there that a depreciation clause in a hire-purchase agreement was a penalty and therefore void. Harman, LJ in a very brief concurring judgment, made this observation: "The Court in my judgment should be slow to interfere with bargains entered into freely and without pressure. I am not satisfied that this bargain can be described as harsh and unconscionable, and unless it passes the test, I am of the opinion that the Court should allow it to stand". Harman LJ seems to have summed up very accurately the essence of the difference between liquidated damages and penalty. The test is by no means easy in application, and is applicable to a large variety of factual situations for which it will be necessary to refer to a tremendous number of cases. We do not propose to do so. It should be, in brief, closely connected with morality which must have much preoccupied the minds of the early Lord Chancellors who were then ecclesiastics or priests at the same time.

Reverting to facts in the instant appeal, what we have is something out of the ordinary. Ordinarily, in provisions for loans of money, if default is made by the borrower, the borrower is made to pay increased interest by means of a higher rate of interest in place of the lower rate of interest prevailing or payable before default. Therefore, arrears arising from default are subject to one SINGLE payment of interest still, though at a higher rate after default. It has been held or approved by the Privy Council that such default interest, if made payable **from** the date of contract, (as distinct from the date of default), always amounts to a penalty. The case in the Privy Council we have in mind is *Sundar Koer v. Sham Kishen* [1906] 341 A 917.

The Privy Council said: "The Indian courts have invariably held that where (as in the present case) the stipulation is retrospective and the increased interest runs from the date of the bond and not merely from the date of default, it is always to be considered as a penalty, **because an additional money payment in that case becomes immediately payable** by the mortgagor. Their Lordships accept this view of the statute" (Emphasis is added). The bold words are crucial to the instant appeal, more of it later. We, on our part, equally accept the same view.

In that case, questions arose in the taking of accounts between a mortgagor and a mortgagee, as to whether certain interest should be allowed. There was a provision in the mortgage for payment of increased interest of 12% p.a. (from the stipulated previous rate of 10½ p.a.) on the money lent to be chargeable and made payable from the date of the execution of mortgage bond till the date of payment should the mortgagor make default in paying interest on the money lent within one year. It was argued that it was a penalty within the meaning of the said section. Such argument was accepted and the Privy Council made the *dictum* quoted above.

It will be noticed that although the increased rate of 12% p.a. was by no means exorbitant, but the provision was held to be void since such default interest would be calculated from the date of the mortgage (though the default took place quite some time after the date of the mortgage) and not from the date of default. The rub was the additional money payment in that case because it became immediately payable by the mortgagor on default. The "additional money payment" was that default interest payable at 12% p.a. from the date of the mortgage to the date of default, and it must have been considered, by implication, as harsh or unconscionable.

Reverting to the instant appeal and having regard to what has been stated in the Privy Council, we have, in hand, the element of "additional money payment" involved also, in that on default, a default interest of 20% p.a. chargeable separately and additionally on arrears comprising principal and interest, became payable. It will be clear from the evidence eg, at p. 153 of the Appeal Record that the default interest of 20% p.a. was paid, side by side with the interest calculated by prescribed rate of interest of 14.5% p.a. on the same money lent or owed for the same span of time. In other words, a second additional payment of interest on the same money lent or owed, and it became payable in addition to the normal payment of interest on the same money lent or owed at 14.5% p.a. well within the ambit of the *ratio* from the *Sundar Koer* case *supra*.

We therefore hold that clause 3.2 of the annexure to the charge in question is void and unenforceable by virtue of s. 75 of the Contracts Act, 1950 and the interest calculated by virtue of the clause 3.2 is irrecoverable.

The next question is whether in such event the chargee is entitled to receive a "reasonable compensation not exceeding ... the penalty stipulated for", according to the said s. 75 which has been judicially interpreted in *Selva Kumar, supra.* We know that there is an established measure of damages payable by a borrower in such default, which is damages for loss of use of fund or money. Such money in the instant case is the sum of money (comprising principal including capitalized principal and interest not yet capitalized) which was in arrear as to evoke (futilely in the instant case), clause 3.2 for charging default interest. Such sum in arrear, if it had not been in

arrear and had been paid back punctually to the chargee could have been lent to some other person by the chargee – at certain rate of interest for the period while it was in arrear.

Damages for the loss of use of such money has not been proved in this case, so that the Court cannot make any award in regard to it following the case of *Kumar, supra.*

In view of the Court finding clause 3.2 void and the said failure to prove damages for loss of use of the money in question, the default interest charged by virtue of the said clause 3.2 would have to be deducted from the amount of repayment to the chargee by the chargor.

About the propriety of the legal fees and costs said to be made payable by clause 10.6 to the same annexure, and raised by the chargor in argument before us, it has not been pleaded in the memorandum of appeal and no attempt was made to amend it for this purpose. In the Court below, the point was barely touched on by both sides and the grounds of judgment of the Court below, have not even mentioned it. On appeal, learned Counsel for the chargor raised it and the opposing Counsel argued against it in a very impromptu and insufficient manner. In the circumstances, in particular, being deprived of the benefit of the learned Judge's view on it, and it not having been pleaded in the memorandum of appeal, we decline to decide thereon and would leave it to another day in an appropriate case.

The learned Judge has made an order in terms of the originating summons dated 10 July 1989 (encl. 1) and prayer (1) therein refers to the outstanding sum of RM6,827.805.43 as at 31 December 1988. The default interest calculated by virtue of the said clause 3.2 would have to be deducted therefrom and the amount so deducted would have to be refunded if it had already been paid to the chargee earlier.

We make the following order:

(1) that the appeal be dismissed save as follows:

(a) that the amount of default interest computed by virtue of clause 3.2 of the annexure to the charge in question be deducted from the sum of RM6,827.805.43 as stated in prayer (1) of the originating summons herein dated 10 July 1989;

(b) that such amount for such deduction be agreed by both parties within one month from the date hereof, failing which the Deputy Registrar of the High Court in question on application by either party, be authorized to determine such amount with an appeal to the Judge-in-Chambers if the determination is disputed; and

(c) that such amount, if already paid to the respondent, be refunded within one week from the date of its ascertainment with interest at 4% p.a. from 10 April 1992 (the date of the order appealed from) to the date of this order, and thereafter at 8% p.a. to date of refund;

(2) that the appellant do pay the respondent 1/2 of the costs of this appeal; and

(3) that the deposit be paid towards the costs but surplus, if any, be referred to the appellant.

Reported by W.A. Sharif